Weighted Guidelines

Cost Efficiency Factor

Cost Efficiency

- Provides additional profit $ for reduction in costs on the “pending” contract
- Range is 0 – 4%
- There is no normal value – start at 0
- Contractor must provide justification with the proposal so it can be analyzed at the same time as other elements
- CO evaluates benefits to specific contract and assigns %

Approach to Analyzing WGL Cost Efficiency

- Step 1 – Top level review of contractor's justification package
  - eliminate any generic, superficial, inconsequential, ambiguous, etc. info that does not demonstrate a specific cost impact to your contract

Examples "We have a cost savings program to reduce overheads and therefore deserve 2% cost efficiency."

"Historically the Program has implemented cost reductions resulting in the average cost coming in under contract cost."

Approach to Analyzing WGL Cost Efficiency

- Step 2 – Review rationale for potential cost savings measures
  - Is the cost savings reflected in the cost line?
  - What is the basis for the estimate?
  - How realistic are these savings?
  - What is likely impact to your contract?

Example “This new machine will save 10,000 hours at $80/hour for a total of $800,000”

Approach to Analyzing WGL Cost Efficiency

- Step 3 – Calculate cost impact to your contract (could be a number of initiatives added together)
  - Savings should be consistent on the cost side and that quantified for cost efficiency

Example: Government believes machine will save 8,000 hours at $80/hour or $640,000 on Contract F33657-02-C-0000/P00001

Approach to Analyzing WGL Cost Efficiency

- Step 4 – Determine Ktr share of cost savings
  - How much should the government share and how much should the contractor share?
  - Consider cost to obtain savings (direct and indirect)
  - Remember that increasing profit % improves contractor return on investment, even though cost baseline may be less
  - Don’t lose sight of big picture
  - This involves judgment

Example: Contractor’s share of $640,000 is $192,000 (based on 70/30 share)

Approach to Analyzing WGL Cost Efficiency

- Step 5 – Translate contractor share into % of cost to determine cost efficiency %
  - Take contractor share and divide by cost dollars (before cost of money)

Example: $192,000/$19,167,382 is 1.0%

Application to Contract Types

- DFARs 215.404-71-5, Cost Efficiency, does not address contract types
- Risk is a major consideration for application
- FFP: Contractor has all the risk if savings do not occur
- FPIF & CPIF: Risk is shared, therefore, share ratio will contribute to decision on amount of efficiency dollars for contractor

Application to Contract Types

- CPFF: Gov’t has all the risk, therefore, no cost efficiency dollars because the savings may not occur thus the gov’t would pay additional fee and the cost

Summary

- There is no normal value – start at 0, until proven otherwise
- The savings must relate to the contract you are negotiating
- Think in terms of dollars, not just percentages
  - 2% of $100,000,000 is $2,000,000
  - 2% of $1,000,000 is $20,000
  - What is the magnitude of the savings?

Summary

- Keep record of cost efficiency packages and resulting savings
  - Methodology should be consistent for same cost initiatives in future

Summary

- Content of Cost Efficiency Packages may duplicate support for other factors of Weighted Guidelines
- Examples from Management/Cost Control Criteria:
  - Does the contractor have an aggressive cost reduction program that has demonstrable benefits?
  - Does the contractor use a high degree of subcontract competition?
  - Does the contractor aggressively seek process improvements to reduce costs?
- Conclusion: Contractors may be better served supporting other factors rather than Cost Efficiency where savings need to be related to pending contract.